

June 2007

DEFENSE CONTRACTING

Use of Undefined Contract Actions Understated and Definitization Time Frames Often Not Met



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Highlights of [GAO-07-559](#), a report to congressional committees

Why GAO Did This Study

To meet urgent needs, the Department of Defense (DOD) can issue undefinitized contract actions (UCA), which authorize contractors to begin work before reaching a final agreement on contract terms. The contractor has little incentive to control costs during this period, creating a potential for wasted taxpayer dollars.

Pursuant to the House of Representatives report on the National Defense Authorization Act for Fiscal Year 2007, we assessed (1) the level of insight DOD has into its use of UCAs, (2) how and when DOD is using UCAs, (3) whether DOD is definitizing UCAs in a timely fashion, and (4) whether contracting officers are documenting the basis for negotiated profit or fee. GAO reviewed 77 randomly-selected contracts at seven locations and interviewed DOD officials.

What GAO Recommends

GAO recommends that the Secretary of Defense take actions to help ensure UCAs are definitized on time and to mitigate associated risks. GAO also recommends that the Administrator of the Office of Federal Procurement Policy, which sets government contracting requirements, improve the level of information needed to oversee UCAs. In written and oral comments, respectively, DOD and the Office of Federal Procurement Policy agreed with the recommendations.

www.gao.gov/cgi-bin/getrpt?GAO-07-559.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Ann Calvaresi-Barr at (202) 512-4841 or calvaresibarra@gao.gov.

DEFENSE CONTRACTING

Use of Undefinitized Contract Actions Understated and Definitization Time Frames Often Not Met

What GAO Found

DOD faces a potentially large gap in its data and thus does not know the extent to which it is using UCAs. DOD's reported obligations for UCAs increased from \$5.98 billion in 2001 to \$6.53 billion in 2005. However, the government's procurement system does not identify undefinitized task or delivery orders or undefinitized contract modifications. In light of DOD's reported increase in its use of task and delivery orders in recent years, the data gap could be large. Because DOD decentralizes oversight of its UCAs, the department would have to manually obtain data from each of its local commands in order to obtain a complete picture. The local commands GAO visited performed oversight of their UCAs to varying degrees.

DOD is generally using UCAs to rapidly fill urgent needs, as permitted, in a variety of circumstances. Local managements' message to the contracting community is to not use a UCA unless absolutely necessary, but this message is emphasized differently from one location to another. GAO found 10 instances in the 77 UCAs we reviewed where UCAs could have been avoided with better acquisition planning. For example, one UCA for the continuation of ongoing services was awarded the day after the previous contract expired.

DOD did not meet the definitization time frame requirement of 180 days after award on 60 percent of the 77 UCAs reviewed. The most common reasons for the delays were untimely receipt of an adequate proposal from the contractor, acquisition workforce shortfalls, and changing requirements. GAO also found that DOD tends to obligate the maximum amount of funding permitted—up to 50 percent of the not-to-exceed amount—immediately at award of UCAs. As a result, contractors may have little incentive to quickly submit proposals. In addition, since DOD does not track whether it meets the Federal Acquisition Regulation requirement to definitize letter contracts (one type of UCA) before 40 percent of the work is complete, GAO was unable to assess compliance with this requirement.

Contracting officers are not documenting, as required, the basis for the profit or fee prenegotiation objective and the profit or fee negotiated. As such, it is unclear whether the costs incurred prior to definitization are considered when computing the profit rates or fee amounts. For the 40 fixed-price contracts GAO reviewed, profit ranged from 3 to 17 percent, and for the 37 cost-type contracts in our sample, fees ranged from 4 to 15 percent. Generally the rate was applied equally over the entire contract term, including the undefinitized period.

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Abbreviations

DFARS	Defense Federal Acquisition Regulation Supplement
DOD	Department of Defense
FAR	Federal Acquisition Regulation
FPDS-NG	Federal Procurement Data System—Next Generation
IG	Inspector General
OFPP	Office of Federal Procurement Policy
UCA	Undefinitized Contract Action

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United States Government Accountability Office
Washington, DC 20548

June 19, 2007

The Honorable Carl Levin
Chairman
The Honorable John McCain
Ranking Member
Committee on Armed Services
United States Senate

The Honorable Ike Skelton
Chairman
The Honorable Duncan Hunter
Ranking Member
Committee on Armed Services
House of Representatives

To meet urgent needs, the Department of Defense (DOD) can authorize contractors to begin work and incur costs before reaching a final agreement on contract terms and conditions, including price. Such agreements are called undefinitized contract actions (UCA). The terms and conditions of UCAs are generally required to be definitized within 180 days, before more than 50 percent of the estimated contract price is obligated, or before more than 40 percent of the work is completed, whichever occurs first.¹ Although UCAs may be necessary to support urgent needs, these actions are not a desirable form of contracting. The government bears the majority of the cost and risk during the undefinitized period. The government risks paying increased costs during this period because the contractor has little incentive to control costs, creating a potential for wasted taxpayer dollars. Therefore, DOD needs to ensure that it is using UCAs only when necessary and that these contract actions are then negotiated as quickly as possible.

The House of Representatives report on the National Defense Authorization Act for Fiscal Year 2007 required us to review whether DOD is properly using UCAs and negotiating them on time.² Accordingly, we

¹The 40 percent requirement as set forth in Federal Acquisition Regulation (FAR) 16.603-2 (c) (3) applies to letter contracts, one type of UCA.

²H.R. Report No. 109-452, p. 353, May 5, 2006.

assessed (1) the level of insight DOD has into its use of UCAs, (2) how and when DOD is using UCAs, (3) whether DOD is definitizing UCAs in a timely fashion, and (4) whether contracting officers are documenting the basis for negotiated profit or fee.

For the purposes of this report, we define UCAs as including letter contracts, undefinitized task and delivery orders,³ and undefinitized contract modifications (that is, modifications that significantly expand or otherwise change the scope of the work). To determine the level of insight DOD has into its use of UCAs, we analyzed information from the DOD DD350 procurement database and interviewed senior-level acquisition officials. We also met with officials from the Office of Management and Budget's Office of Federal Procurement Policy (OFPP) to discuss the data available for oversight of UCAs. OFPP is responsible for collecting, developing, and disseminating government procurement data. The most significant governmentwide data collection tool is the Federal Procurement Data System-Next Generation (FPDS-NG).⁴ To identify how and when DOD is using UCAs and whether DOD is definitizing these actions in a timely manner, we reviewed a randomly selected sample of 77 UCAs from the six military locations that awarded the majority of dollars for letter contracts during fiscal years 2004 and 2005 and one non military defense agency that issued several UCAs during that time period. The specific locations selected for our review were

- Air Force: Aeronautical Systems Center and Warner Robins Air Logistics Center,
- Army: Aviation and Missile Command and TACOM Life Cycle Management Command,
- Navy: Naval Air Systems Command and Naval Sea Systems Command, and
- National Geospatial-Intelligence Agency.

For purposes of this report, we refer to these seven locations as the local commands.

³Task and delivery orders are placed against a preexisting contract for supplies or services that does not procure or specify a firm quantity (other than a minimum or a maximum quantity) and that provides for the issuance of orders for the delivery of supplies or performance of tasks during the period of the contract. FAR 16.501-1.

⁴Beginning with fiscal year 2007, DOD's procurement data are fed directly into the FPDS-NG; the DD350 database is no longer separately maintained.

At each location, we reviewed contract files and interviewed officials from the local acquisition office as well as the contracting officers responsible for the UCAs we reviewed and selected program office officials. We also reviewed relevant federal and defense acquisition regulations regarding the appropriate use of and definitization requirements for UCAs. In addition, we interviewed representatives from four companies who entered into UCAs with either military services or the National Geospatial-Intelligence Agency. Appendix I provides details on our scope and methodology and Appendix II lists the contracts and orders we reviewed. We conducted our work from August 2006 through April 2007 in accordance with generally accepted government auditing standards.

Results in Brief

DOD faces a potentially large gap in its data and thus does not know the extent to which it is using UCAs. DOD's reported obligations for UCAs increased from \$5.98 billion in fiscal year 2001 to \$6.53 billion in fiscal year 2005. However, the government's procurement system does not identify undefinitized task or delivery orders or undefinitized contract modifications. In light of DOD's reported increase in its use of task and delivery orders in recent years, the data gap could be large. For example, one location we visited had 91 undefinitized orders with \$525 million in obligations during fiscal years 2004 and 2005. Given the manner in which the data are recorded, these orders would not be identified, at award, as UCAs in the procurement system. Because DOD's oversight of its UCAs is decentralized, the department would have to manually obtain data from each of its local commands in order to obtain a complete picture. The local commands we visited performed oversight of their UCAs to varying degrees.

DOD is generally using UCAs to rapidly fill urgent needs, as permitted, in a variety of circumstances at the locations we visited. The local managements' message to the contracting community is to not use a UCA unless absolutely necessary. However, this message seems to have resonated to different degrees with the frontline acquisition staff who requested and awarded the UCAs we reviewed. The UCAs we reviewed ranged from providing supplies or services directly to warfighters to procuring long lead items for larger programs.⁵ In fact, about half of the

⁵For purposes of this report, long lead items are defined as those components of a system or piece of equipment for which the times to design and fabricate are the longest, and therefore, to which an early commitment of funds may be desirable in order to meet the earliest possible date of system completion.

77 UCAs we reviewed were for direct or indirect support of ongoing war efforts. The remaining UCAs were generally awarded to maintain program schedules. In addition, 10 of the UCAs we reviewed were attributable to inadequate planning. For example, one UCA for the continuation of ongoing services was awarded the day after the previous contract expired.

DOD did not meet the definitization time frame requirement of 180 days after award on 60 percent of the UCAs we reviewed. On average, the military services took an additional 2 months, and the National Geospatial Intelligence Agency took about 3½ extra months to definitize its UCAs. Sixteen of the UCAs we reviewed had remained undefinitized for a year or more. Contracting officers cited many reasons for the delays, but the most common were untimely receipt of an adequate proposal from the contractor, acquisition workforce shortfalls, and changing requirements. Delayed definitization of UCAs transfers additional cost and performance risk to the government, since contractors are normally reimbursed for all allowable costs incurred before definitization. We also found that DOD tends to obligate the maximum amount of funding permitted—up to 50 percent of the not-to-exceed amount—immediately at award of UCAs. As a result, contractors may have little incentive to quickly submit proposals, and agencies have little incentive to demand their prompt submission, since funds are available to proceed with the work. In addition, since DOD does not track whether it meets the Federal Acquisition Regulation (FAR) requirement to definitize letter contracts before 40 percent of the work is complete, we were unable to assess compliance with this requirement.

Contracting officers are not documenting, as required by federal regulations, the basis for the profit or fee prenegotiation objective and the profit or fee negotiated. Specifically, they are not generally documenting, when applicable, whether profit or fee is adjusted for work performed by the contractor at a lower level of risk during the undefinitized period. In the absence of such documentation, it is unclear whether the costs incurred prior to definitization are considered when computing the profit rates or fee amounts. For the 40 fixed-price contracts we reviewed, profit ranged from 3 to 17 percent, and for the 37 cost-type contracts in our sample, fees ranged from 4 to 15 percent. Generally the rate was applied equally over the entire contract term, including the undefinitized period.

This report contains recommendations to the Secretary of Defense and the Administrator of the Office of Management and Budget's Office of Federal Procurement Policy that are intended to improve DOD's oversight of its use of UCAs, to help ensure UCAs are definitized on time, and to mitigate

the risks associated with delays in definitization. In written comments on a draft of this report, DOD concurred with the recommendations and noted actions underway that are directly responsive. Officials from the Office of Federal Procurement Policy, in oral comments, agreed with the recommendation to add a data field in FPDS-NG to identify undefinitized orders and contract modifications. DOD's comments are included in appendix III.

Background

DOD is increasingly relying on contractor services to accomplish its missions. In fiscal year 2006, DOD awarded more than \$294 billion in contracts. Despite this huge investment in buying goods and services, our work and the work of the DOD Inspector General (IG) has found that DOD's spending sometimes is inefficient and not managed effectively. Too often, requirements are not clearly defined; rigorous price analyses are not performed, and contractors' performance is not sufficiently overseen. In fact, we have identified overall DOD contract management as a high-risk area for the past several years.

When a requirement needs to be met quickly and there is insufficient time to use normal contracting vehicles, federal regulations permit the use of a UCA. UCAs are binding commitments used when the government needs the contractor to start work immediately and there is insufficient time to negotiate all of the terms and conditions for a contract. UCAs can be entered into via different contract vehicles, such as a letter contract (a stand-alone contract), a task or delivery order issued against a pre-established umbrella contract, or a modification to an already established contract.

The FAR and the Defense Federal Acquisition Regulation Supplement (DFARS) govern how and when UCAs can be used. The regulations also establish requirements as to how quickly UCAs must be definitized. Although each regulation contains two criteria, they are not the same. The FAR states that a letter contract needs to be definitized within 180 days after the award date or before 40 percent of the work is complete, whichever occurs first. While the DFARS includes the 180-day time frame, it addresses all UCAs (including undefinitized task and delivery orders and contract modifications) and adds a requirement to definitize before more than 50 percent of funds are obligated. It does not mention the 40 percent of work completed. Under FAR and DFARS respectively, a waiver of the 180-day requirement can be granted for extreme circumstances or when the agency is supporting a contingency or peacekeeping operation. The definitization time frame can also be extended an additional 180 days

when a qualifying proposal is received from the contractor. The contractor does not receive profit or fee during the undefinitized period, but can recoup it once the contract is definitized.

Under UCAs, the government risks paying unnecessary costs. For example, in a September 2006 report on contracts in support of Iraq reconstruction, we found that the timeliness of definitization can affect the government's costs.⁶ We reported that DOD contracting officials were more likely to adhere to the Defense Contract Audit Agency's advice regarding the disposition of questioned and unsupported costs when negotiations were timely and occurred before contractors had incurred substantial costs under UCAs. On the other hand, contracting officials were less likely to remove questioned costs from a contract proposal when the contractor had already incurred these costs during the undefinitized period. Similarly, the DOD IG found that untimely definitization of contracts transfers additional cost and performance risk from the contractors to the government.⁷

Contractors should bear an equitable share of contract cost risk and receive compensation for bearing additional risk based on the degree of risk assumed. Costs that have already been incurred on an unpriced action, such as a letter contract, have virtually no cost risk associated with them. As such, when negotiating profit with the contractor, the government may attribute a zero risk factor to the undefinitized period.⁸

DOD Does Not Know the Full Extent of Its UCA Usage

DOD faces a potentially large gap in its data and thus does not know the extent to which it is using UCAs. The federal procurement data system is only able to identify UCAs that are awarded via letter contracts. Undefinitized task or delivery orders, as well as contract modifications, are not identified. DOD also lacks high-level oversight of its UCA activity since UCA monitoring has been delegated to the local commands, with upward reporting no longer required. At the local commands we visited,

⁶GAO, *Iraq Contract Costs: DOD Consideration of Defense Contract Audit Agency's Findings*, [GAO-06-1132](#) (Washington, D.C.: Sept. 25, 2006).

⁷Department of Defense, Office of the Inspector General, *Audit Report: Undefinitized Contract Actions*. Report Number D-2004-112, Arlington, Virginia: Aug. 30, 2004.

⁸In addition to contract cost risk, other factors are also considered when determining profit, including the contractor's effort, use of federal socioeconomic programs, capital investments, cost control and other past accomplishments, and independent development.

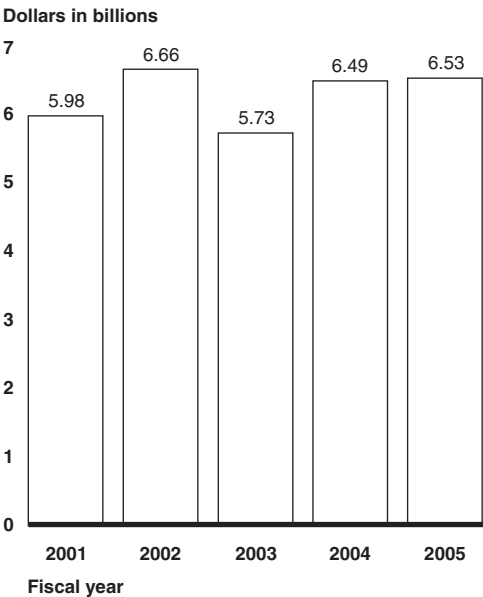
monitoring of UCAs varied in both detail of information and frequency of review.

Data on UCAs Are Incomplete

DOD understates its UCA usage due to a potentially significant gap in data. Because the government’s federal procurement data system—managed by the Office of Federal Procurement Policy—only identifies letter contracts as undefinitized at award and does not identify undefinitized task or delivery orders or contract modifications, DOD does not know the extent of its UCA activity.⁹

As figure 1 shows, DOD’s reported obligations for letter contracts have increased from \$5.98 billion in fiscal year 2001 to \$6.53 billion in fiscal year 2005. These obligations for letter contracts as a percentage of DOD’s total obligations remained 4 percent or less during this time period.

Figure 1: DOD Reported Obligations on Letter Contracts for Fiscal Years 2001-2005

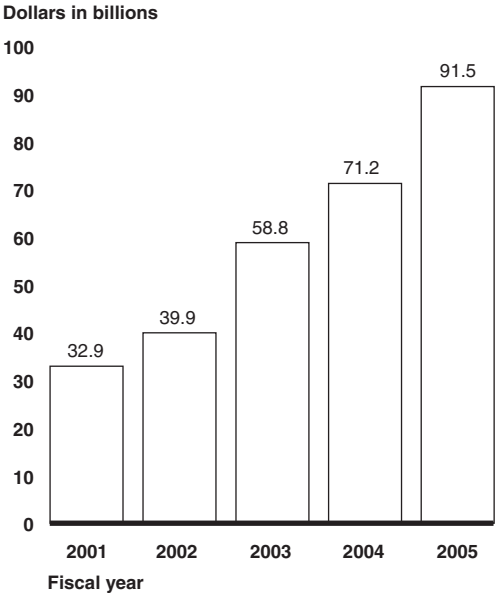


Source: GAO analysis of DD350 data.

⁹This same issue also pertains to other federal agencies. However, we are limiting our discussion to DOD because that agency is the focus of this report.

At the same time, DOD's task and delivery order obligations have increased significantly, as shown in figure 2.

Figure 2: DOD Obligations on Task and Delivery Orders for Fiscal Years 2001-2005



Source: GAO analysis of DD350 data.

A DOD senior acquisition official stated that if DOD wanted to know the amount obligated under undefinitized task and delivery orders, it would have to ask for the information from all of the local commands. According to information maintained at the local commands we visited, most have issued some undefinitized task or delivery orders. As table 1 illustrates, one command obligated over \$500 million in UCA orders during the 2-year period we reviewed.

Table 1: Obligations on Unfinalized Task and Delivery Orders during Fiscal Years 2004-2005 at Locations Visited

Location	Obligations (dollars in millions)	Number of actions
Aeronautical Systems Center	\$524.7	91
Aviation and Missile Command	81.0	12
Naval Air Systems Command	8.0	5
Naval Sea Systems Command	49.3	1
Warner Robins Air Logistics Center	14.9	2
Total	\$677.9	111

Source: GAO analysis of DOD data.

Note: The Army's TACOM Life Cycle Management Agency Command reported no UCA orders during this period. The National Geospatial-Intelligence Agency had unfinalized orders during this period but does not track this information for its DOD contracts.

DOD Lacks Centralized Oversight of UCAs

UCA oversight takes place at local commands, without any centralized reporting at the DOD headquarters or military services levels. Although UCA oversight was centralized in the past, a senior DOD acquisition official told us that DOD does not believe that UCA usage is a significant concern, given that letter contracts have represented no more than 4 percent of DOD's total obligations over the past several years. As such, DOD relies on its local commands to oversee the use of UCAs and inform upper management if any issues arise.

The Air Force is the only military service that has a reporting requirement for UCA activity. A June 2002 policy requires commands to report to the headquarters acquisition office on UCAs that have remained unfinalized for more than 1 year. However, the acquisition office has not received any reports on delinquent UCAs, despite the fact that we found 9 UCAs that had remained unfinalized for over 1 year at the two Air Force commands we visited. An official from one of the commands told us it reported one of its delinquent UCAs, but, according to an Air Force headquarters acquisition official, it was never received. Since the reporting of delinquent UCAs is by a manual self-reporting system, it is possible that other delinquent UCAs have gone unreported.

The local commands we visited performed oversight of their UCA usage to varying degrees. All of the military locations had some sort of reporting of UCA activity to the local acquisition management on a regular basis, ranging from monthly to quarterly reporting. The local commands also

varied in whether all UCAs were tracked versus only those that remain undefinitized after the 180-day time frame. We found that the National Geospatial-Intelligence Agency was not tracking or monitoring its DOD UCAs,¹⁰ even though its acquisition regulation requires a monthly report on UCA activity.¹¹ After we raised this issue, National Geospatial-Intelligence Agency officials stated that they will begin monitoring their UCA activity.

UCAs Used to Quickly Fill Needs in a Variety of Circumstances

DOD is using UCAs to rapidly fill needs in a variety of circumstances, many of which are directly or indirectly related to the war in Iraq. The message from management at the locations we visited is to limit the use of UCAs. However, this message seems to have resonated to different degrees with the frontline acquisition staff who requested and awarded the UCAs we reviewed. In some instances, inadequate acquisition planning drove the need for the UCA.

UCAs Are Awarded for a Variety of Goods and Services

The UCAs we reviewed were for a range of goods and services—from providing immediate support to the warfighter in theater to procuring long lead items to keep weapon system program schedules on time. The military services' commands awarded about half of the UCAs we reviewed for support of war efforts and one third to meet schedules on production contracts. In one instance, a UCA was awarded to immediately provide body armor on combat vehicles already in use in operations in the Middle East. In another, a UCA was awarded to obtain a jamming system that was needed to avoid grounding F-15 aircraft. The National Geospatial-Intelligence Agency awarded over half of the UCAs we reviewed for immediate intelligence needs and about half to avoid disruptions of services it was receiving under expiring contracts.

Table 2 provides a summary of the reasons presented by the contract files and discussed with the contracting officers specifically for the 77 UCAs we reviewed.

¹⁰The National Geospatial-Intelligence Agency also has authority to contract under the Central Intelligence Agency's procurement authority; our review included the agency's DOD activity only.

¹¹National Geospatial-Intelligence Agency Instruction for Acquisition Regulation Implementation 5X217.7403-91.

Table 2: Reasons Cited for Issuance on UCAs Reviewed

Reasons for issuance of UCA	Number of instances
Maintaining program schedules	28
Direct support of war efforts	22
Indirect support of war efforts (e.g. replacing depleted spare parts)	16
Timing of funding	11
Inadequate acquisition planning	10
Other	12

Source: GAO analysis of DOD data.

Note: We reviewed 77 UCAs. However, multiple reasons were cited for the same action. “Other” reasons include actions to avoid costs for future upgrades or changes required due to factors external to the program office.

Poor acquisition planning is not an appropriate reason to award a UCA. However, for 10 of the UCAs we reviewed, the government may have been able to prevent the use of a UCA with better planning. These included, for example, 4 UCAs issued to procure long lead items that could have been contracted for earlier. The requirement for long lead items is typically established early in a program and is normally provided advanced funding in the annual budget process, which should provide sufficient time to acquire the items through normal acquisition procedures. Other inadequate planning situations included 4 UCAs—1 at the Naval Sea Systems Command and 3 at the National Geospatial-Intelligence Agency—that we believe could have been prevented by the program office. In each instance, the requirement was known in a significant amount of time before the UCA was issued. These situations ranged from late issuance of the request for proposals (which had been planned earlier) to awards that were issued quickly to avoid disruptions in services (which could have been anticipated). For example, one National Geospatial-Intelligence Agency UCA for the continuation of ongoing services was awarded the day after the services from the prior contract ended. The agency should have been able to reasonably estimate the requirement and prices in advance based on the terms and work of the ongoing contract, which were already known. The remaining three inadequate planning situations were due to circumstances that were beyond the control of the program office. For example, a Navy UCA was issued because the senior acquisition executive, external to the program office, delayed the approval of the program’s acquisition plan. Furthermore, one UCA added requirements that expanded the work beyond what was originally planned. Specifically, the National Geospatial-Intelligence Agency awarded a UCA to quickly obtain

aerial data from the regions affected by hurricanes, but subsequently augmented it to establish a permanent facility that had been planned for some time. Several contracting officers across DOD expressed concern that program office staff need training on the appropriate use of UCAs because they do not always seem to be aware of the risks that these contract actions pose to the government.

Local Command Policies Generally Focus on Limiting UCAs

The “tone at the top” provided by the local commands we visited is to not use UCAs unless absolutely necessary. However, this message is emphasized differently from one location to another and has only recently come about in some locations. For example, an April 2000 Naval Air Systems Command memorandum says that the use of UCAs is to be kept to the “absolute minimum” and that they should not be used if the requirements are not fully defined. On the other hand, the National Geospatial-Intelligence Agency allowed its contracting officers to use UCAs without the need for higher-level approval until a May 2006 memorandum elevated the approval authority to the senior procurement executive.

Representatives from the four companies we spoke with use UCAs with DOD to different degrees—ranging from considering UCAs to be a “normal part of business” to rarely using UCAs in recent years. One company said that its UCAs are mostly used for short duration work needed to maintain critical schedules in the development or production processes of other contracts. Another company recently entered into several indefinite delivery/indefinite quantity contracts with the government so that UCAs could be avoided in that area of work.

DOD is Often Not Meeting Definitization Time Frame Requirements

DOD did not meet the definitization time frame requirement of 180 days after award for over half the UCAs we reviewed. This situation places the government at risk of paying increased costs, thus potentially wasting taxpayers’ money. On average, the UCAs we reviewed were definitized more than 2 months past the required period, with 16 remaining undefinitized for a year or more. While DOD regulations allow up to half of the funding to be provided before definitization, we found that DOD tends to obligate this maximum amount of funding immediately at award—a practice that could provide a disincentive for the timely definitization of the UCA. In addition, DOD does not monitor its compliance with the FAR requirement to definitize letter contracts when 40 percent of the work is complete.

Most UCAs Were Not
Definitized within
Required Time Frames

Sixty percent of the UCAs we reviewed—46 of 77—were not definitized within the 180-day time frame required by FAR and DFARS. Table 3 shows the number of days elapsed before the UCAs were definitized.

Table 3: Elapsed Days before Definitization on UCAs Reviewed					
	Days until definitized				Total
	0-180	181-365	366-500	Over 500	
Air Force	12	7	3	2	24
Army	10	9	3	1	23
Navy	7	11	5	0	23
National Geospatial-Intelligence Agency	2	3	2	0	7
Total	31	30	13	3	77

Source: GAO analysis of DOD data.

We found 16 UCAs that took more than a year to definitize, with the longest taking over 600 days. Each location we visited had at least 1 UCA in effect for over a year. In addition, we found no discernable relationship between the dollar value or contract type of the UCAs and the length of time it took to definitize. Approximately the same proportion of small and large dollar value UCAs were definitized in less than 180 days as were definitized in more than 180 days. Likewise, the final contract type did not appear to influence the timeliness of definitization. Approximately the same proportion of UCAs with final contract types of fixed-price and cost-type were definitized in less than 180 days as were definitized in more than 180 days.

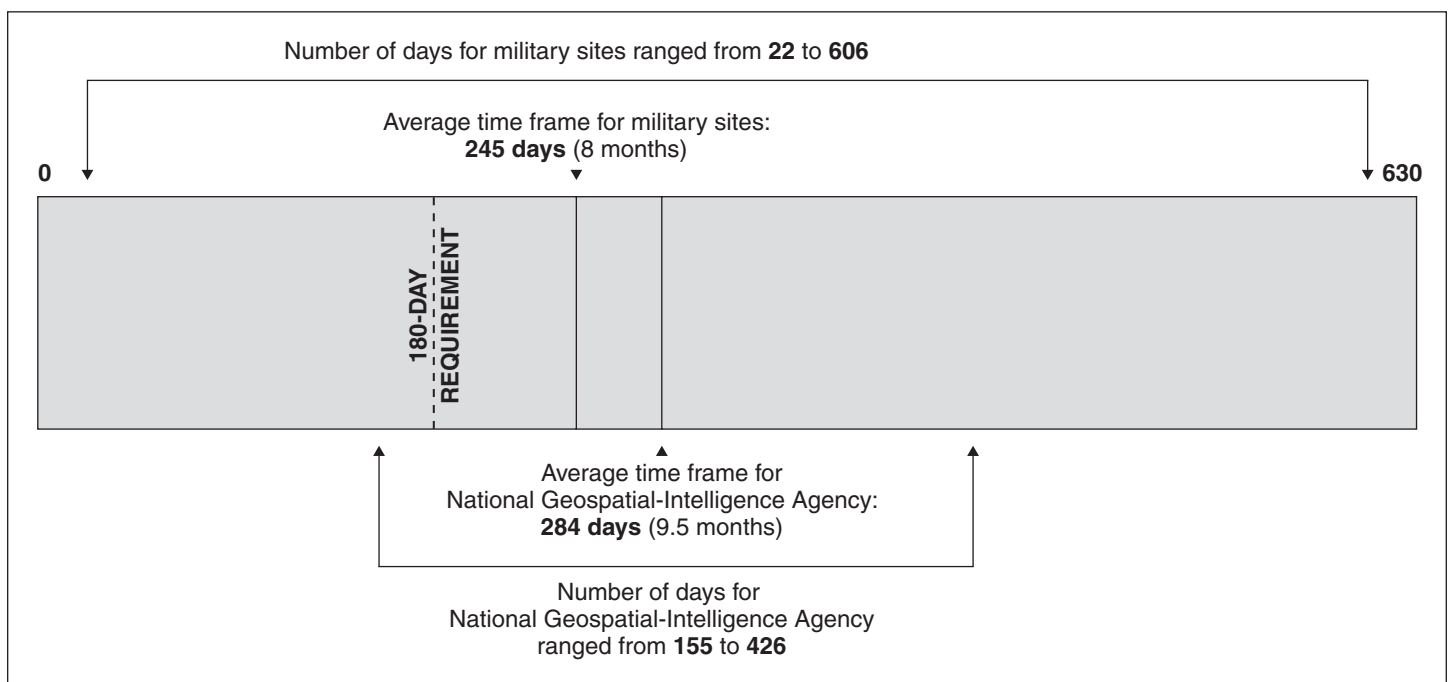
We also identified a number of UCAs that met provisions that allow an extension or waiver of the 180-day definitization requirement. FAR and DFARS allow an additional 180-day extension of the definitization time frame from the date a qualifying proposal (one that is complete and auditable) is received from the contractor.¹² Our review showed that definitization occurred during this extended time frame in only 7 of the 36 cases. Two UCAs were permitted waivers of the 180-day requirement since they were in support of contingency operations, pursuant to a

¹² A “qualifying proposal” means a proposal containing sufficient information for DOD to do complete and meaningful analyses and audits of the information in the proposal and any other information that the contracting officer has determined DOD needs to review in connection with the contract. DFARS 217.7401(c).

September 2003 Air Force memorandum waiving the time frame for actions related to Operation Iraqi Freedom.

Figure 3 illustrates the average time frames and the range of days that lapsed before definitization.

Figure 3: Average Time Frame for Definitization of UCAs



Source: DOD (data); GAO (analysis and presentation).

Note: The average time frame includes 9 UCAs that took more than 180 days to definitize but were provided extensions due to receipt of a qualifying proposal or were authorized waivers when the requirement was for contingency operations.

Delays in Definitization Occur for a Variety of Reasons

Contracting officials provided more than a dozen reasons for not definitizing UCAs within the original 180-day time frame. Based on our review of the contract files and discussions with contracting and program officials, the most common reasons for the delays were (1) delays in obtaining a qualifying proposal from the contractor, (2) acquisition workforce shortages that led to overly heavy workloads, and (3) complexity of requirements at award of the UCA or changing requirements after award. In many cases, multiple reasons contributed to the definitization delay. Some of the longest delayed definitizations occurred because of a combination of the three reasons stated above.

Table 4 provides a summary of the number of instances each reason was provided as an explanation of the delay.

Table 4: Definitization Delays Cited for UCAs Reviewed

Reasons for delays	Number of instances
Untimely receipt of qualifying proposal	23
Government acquisition workforce shortages/workloads	11
Changing or complex requirements	10
Changes in funding availability	6
Contracting officer's inadequate performance	4
Required audits	4
Protracted negotiations	3
Hurricanes	3
Other	13

Source: GAO analysis of DOD data.

Note: "Other" reasons include data rights issues, waiting for program milestone decisions, and delays in obtaining certified cost and pricing data.

Contracting officers stated that delays in obtaining a qualifying proposal were sometimes caused by the program office's changing requirements. Many contracting officials stated the government's requirement was inadequately described when the UCA was awarded or was subsequently changed after award once the requirement was better understood. Contractor representatives and contracting officers noted that it is difficult for a contractor to timely submit an adequate proposal when the government is unsure about the specifications of the product or service it requires. Officials at two companies noted that they attempt to submit qualifying proposals on time, but must redo them—sometimes multiple times—to reflect the government's revised requirements.

In addition to timeliness of proposals and changing requirements, shortfalls in the government's acquisition workforce were another key reason for definitization delays. This issue was manifest in different ways, including inadequate numbers of contracting officials, the heavy workload of the Defense Contract Audit Agency, which is frequently called upon to perform audits of the proposal's pricing structure, and, in four cases, contracting officials who did not perform their duties to definitize the UCAs. Some contracting officers commented that UCAs require twice the work that a normal contract award does, because in essence they go through the contracting process twice—once for the undefinitized period

and once for the definitized period. Problems with acquisition staff or workloads at the commands resulted, in some instances, in a UCA remaining undefinitized until someone turned attention to it. Some contracting officers told us that their focus is on getting the UCA awarded; after that, they often must turn to other pressing awards so that following up on definitizations becomes less of a priority. We also found one situation where a UCA simply fell through the cracks because it dropped off the local reporting system due to a computer error. In one case, the contracting officer awarded a UCA but took another job before it was definitized, and the contracting officer who inherited it was not aware for some time that it had not been definitized; thus, no one acted on it for over a year.

UCAs Are Usually Awarded with Maximum Obligations Allowed

Most of the UCAs we reviewed were awarded with the maximum obligations allowed. Specifically, 60 of the 77 UCAs—78 percent—were obligated with approximately 50 percent or more of the not-to-exceed price at award. As a result, contractors may have less incentive to hasten the submission of qualifying proposals and agencies have little incentive to demand their prompt submission, since funds are available to proceed with the work, leading to a protracted negotiation process. One contracting officer obligated a smaller percentage initially, but as time went by and various issues arose that slowed definitization, he raised the obligated amount little by little until it reached 50 percent. In hindsight, he said it would have been easier to just obligate the 50 percent at the beginning. Company officials said that the minimum amount needed to begin work under a UCA depends on the circumstances of the work. Officials from all four companies told us they usually receive 50 percent of the not-to-exceed price at award.

While we found some evidence of monitoring the percentage of funds obligated, in accordance with the DFARS requirement to definitize UCAs before 50 percent of the funding is obligated, none of the commands we visited act proactively to ensure the obligations do not exceed this maximum amount. As a result, DOD is at risk of increasing the potential that it is paying additional unnecessary costs during the undefinitized period. The monitoring that does occur, at three local commands we visited, is not effective in ensuring compliance with the requirement because no alerts are generated if a UCA goes beyond the maximum obligations before definitization. An official at one command that does not monitor this requirement stated that the command does not do so because it is the responsibility of the contracting officer to ensure it is met.

Requirement to Definitize Before 40 Percent of Work Is Completed Is Not Tracked

DOD is not monitoring compliance with the FAR requirement to definitize letter contracts when 40 percent of the work is complete. None of the local commands we visited had procedures in place to track this provision. Officials at two commands were not familiar with the requirement. As such, we were unable to assess whether DOD is in compliance with this requirement. Many contracting officers stated that the amount of work completed before definitization could not readily be determined because under a UCA there is no established baseline against which to measure the percentage of work completed. Policy officials at several locations we visited also stated that the FAR requirement would be difficult to implement. Based on our findings, a DFARS case was initiated in April 2007 to clarify defense acquisition regulations.

Little Insight into Whether Reduced Risk Is Taken into Account when Negotiating Profit or Fee

Contracting officers are not usually documenting, when applicable, whether profit or fee is adjusted for work performed by the contractor at a lower level of risk during the undefinitized period. All UCAs are essentially cost-reimbursement contracts until definitized, as contractors are reimbursed for all incurred costs that are reasonable, allocable, and allowable during the undefinitized period. This contract type places the greatest cost risk on the government. When the UCA is definitized, the ultimate contract type is determined. Our sample included a variety of final contract types, including firm-fixed-price, cost-plus-award-fee, cost-plus-incentive-fee, and cost-plus-fixed-fee. Each contract type includes either profit (fixed-price contracts) or fee (cost-type contracts) for the contractor. During the undefinitized period, however, profit or fee is not paid. The profit rate or fee is derived at definitization and then applied across the entire period of performance, including the undefinitized period.

When calculating the negotiating position on profit or fee for a UCA, the FAR and DFARS require contracting officers to assess the relative risk borne by the contractor versus the government. The amount of profit or fee available to the contractor is usually determined via a structured calculation that is a function of several different factors, such as the complexity of the work, resources required to perform, independent efforts by the contractor to bring about improved performance, and contract type. Specifically, the DFARS states that when determining a profit or fee position during negotiations to definitize a UCA, contracting officers must consider any reduced risk on the portion of the contract performed before definitization and any reduced risk on the remaining portion that will be performed after definitization. For example, the DFARS states that

“When the final price of a UCA is negotiated after a substantial portion of the required performance has been completed, the head of the contracting activity shall ensure the profit allowed reflects (a) Any reduced cost risk to the contractor for costs incurred during contract performance before negotiation of the final price; and (b) The contractor’s reduced cost risk for costs incurred during performance of the remainder of the contract.”¹³

When costs have been incurred prior to definitization, contracting officers are to generally regard the contract type risk to be in the low end of the designated range. If a substantial portion of the costs have been incurred prior to definitization, the contracting officer may assign a value as low as 0 percent, regardless of contract type.¹⁴

Table 5 shows the range of profit and fee rates negotiated at definitization for the UCAs we reviewed. We did not assess the reasonableness of the profit or fee percentages determined by the contracting officers.

Table 5: Range of Negotiated Profit or Fee Rates for UCAs Reviewed

	Profit or fee percentage			
	Fixed-price		Cost-type	
	Low	High	Low	High
Air Force	3.0	15.0	5.2	14.5
Army	6.0	17.2	9.0	15.0
Navy	7.9	13.9	7.0	15.0
National Geospatial-Intelligence Agency	none	none	4.0	15.0

Source: GAO analysis of DOD data.

We found that these adjustments to profit or fee were usually not documented in the price negotiation memorandum, a contract document that sets forth the results of the negotiations and contains the contracting officer’s determination that the negotiated price is fair and reasonable. Specifically, the memorandums for only 14 of the 77 UCAs we reviewed discussed how the negotiated profit or fee was affected by the UCA. As a result, for the majority of the UCAs we reviewed, no determination can be made whether the costs incurred during the undefinitized period were considered when the allowable profit or fee was determined. Similarly, in

¹³DFARS 217.7404-6.

¹⁴DFARS 215.404-71-3(d)(2).

a 2004 report, the DOD IG found that contract records did not contain evidence that allowable profit factors, such as the reduced cost risk, were considered in the final profit rate awarded to the contractor. It was also not evident that already incurred costs were taken into account when determining profit.¹⁵

The majority of the contracting officers responsible for the UCAs we reviewed acknowledged that they are required to document how the shift in risk associated with the undefinitized period was accounted for in determining the profit or fee calculated for negotiations.

Conclusions

UCAs are a necessary tool for DOD to use to meet urgent contracting needs, but DOD must ensure that their use is limited to appropriate circumstances. Even when UCAs are used appropriately, increased management attention is needed regarding definitization time frames so the government's position during subsequent negotiations is not overly weakened. Existing regulations and guidance governing UCAs are not always understood or followed. Actions are needed to strengthen management controls and oversight of UCAs; otherwise the department will remain at risk of paying unnecessary costs and potentially excessive profit rates.

Recommendations for Executive Action

To improve oversight of UCAs, we recommend that

- the Administrator of the Office of Management and Budget's Office of Federal Procurement Policy assess whether the Federal Procurement Data System-Next Generation data fields need to be modified to require coding that will identify undefinitized task and delivery orders and undefinitized contract modifications, and
- the Secretary of Defense issue guidance to program and contracting officials on how to comply with the FAR requirement to definitize when 40 percent of the work is complete.

To help ensure that UCAs are definitized in accordance with regulations, we recommend that the Secretary of Defense take the following two actions:

¹⁵DOD IG Report Number D-2004-112.

-
- put in place a reporting channel to headquarters that includes information on UCAs in place for 180 days or more and that outlines plans and time frames for definitization, and
 - supplement acquisition personnel on an as-needed basis to quickly definitize UCAs once they are awarded.

To mitigate the risks of paying increased costs under UCAs, we recommend that the Secretary of Defense set forth supplemental guidance to accomplish the following two actions:

- direct contracting officers, where feasible, to obligate less than the maximum allowed at UCA award to incentivize contractors to expedite the definitization process, and
- specify that the effect of contractor's reduced risk during the undefinitized period on profit or fee be documented in the price negotiation memorandum or its equivalent.

Agency Comments and Our Evaluation

We provided a draft of this report to DOD and the Office of Federal Procurement Policy for comment. In written comments, DOD concurred with our findings and recommendations and noted actions underway that are directly responsive. The department's comments are reproduced in appendix III. The Office of Federal Procurement Policy provided oral comments, stating that it had no concerns regarding our recommendation to add a data field in FPDS-NG that would identify undefinitized task and delivery orders and contract modifications at award. Such data are needed to provide DOD (and other agencies) more complete information on UCAs, which can then be used to improve oversight of their use.

Although DOD concurred with our recommendation to issue guidance addressing the FAR definitization requirement, in its comments, DOD stated that our reference to the FAR requirements for UCA definitization schedules did not consider the difference in requirements for DOD that are specified in the U.S. Code. However, our report does address those differences. DOD also stated that the Defense Acquisition Regulation Council has initiated a DFARS case, based upon our discussions during this review, to clarify that DOD contracting officers should use the DOD definitization schedule criteria. DOD agreed that the need for enhanced oversight of UCAs is appropriate and said it will consider requiring the military departments to enhance oversight of UCAs and to provide periodic reports, with remediation plans, for those past the definitization time frames. The Department also published two notices in the *Federal Register* on May 22, 2007, seeking public comments on current DOD

contract financing and funding policies, including the weighted guidelines that are used to determine appropriate profit or fee based on an assessment of contractor risk.

We are sending copies of this report to the Secretary of Defense, the Director of the Office of Management and Budget, the Administrator of the Office of Federal Procurement Policy, and other interested congressional committees. We will also make copies available to others upon request. In addition, the report will be available at no charge on the GAO Web site at <http://www.gao.gov>.

If you have any questions about this report or need additional information, please contact me at (202) 512-6986 or calvaresibarra@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Key contributors to this report were Michele Mackin, Assistant Director; R. Eli DeVan; Lily Chin; Matthew T. Drerup; Victoria Klepac; John Krump; Jean K. Lee; and Lynn Milan.

A handwritten signature in black ink that reads "Ann Calvaresi Barr". The signature is written in a cursive, flowing style.

Ann Calvaresi-Barr
Director, Acquisition and Sourcing Management

Appendix I: Scope and Methodology

To determine the level of insight the Department of Defense (DOD) has into its use of undefinitized contract actions (UCA), we interviewed DOD senior-level acquisition officials and service-level acquisition officials to identify any additional policies specifically addressing the use of undefinitized contract actions at the locations selected for our review. We analyzed information from DOD's procurement system (DD350) and local commands for undefinitized contract actions from fiscal year 2001 through fiscal year 2005. We also reviewed the relevant sections of the Federal Acquisition Regulation and the Defense Federal Acquisition Regulation Supplement, as well as service-level guidance pertaining to the use of undefinitized contract actions.

To identify how and when DOD is using UCAs and whether DOD is definitizing these actions in a timely manner, we reviewed a random sample of undefinitized contract actions from six military commands and one non military defense agency. While undefinitized contract actions may include letter contracts, task or delivery orders, and contract modifications, only letter contracts are recorded by DD350 in a manner that allowed GAO to identify them as undefinitized at the time of award. Therefore, the specific locations for our review were selected based on the total dollar value and volume of letter contracts issued during fiscal years 2004 and 2005 by various DOD buying organizations as recorded in the DD350 system. On the basis of this data, we selected the two commands with the largest dollar volume of letter contracts within each of the three military services (Air Force, Army, and Navy). As such, the six military locations represented over 75 percent of the total dollars awarded for letter contracts during the period. We also selected the non military defense agency with the largest number of letter contracts. The specific locations selected for our review were:

U.S. Air Force

Aeronautical Systems Center, Dayton, Ohio

Warner Robins Air Logistics Center, Warner Robins, Georgia

U.S. Army

TACOM Life Cycle Management Command, Warren, Michigan

Aviation and Missile Command, Huntsville, Alabama

U.S. Navy

Naval Sea Systems Command, Washington, D.C .

Naval Air Systems Command, Patuxent River, Maryland

Non military defense agency

National Geospatial-Intelligence Agency, Washington, D.C.

To include other types of undefinitized contract actions in our review, we requested a listing of task and delivery order and contract modifications issued as undefinitized contract actions during fiscal years 2004 and 2005 from each of the seven locations that we planned to visit. This request was necessary because these types of undefinitized actions are not identified in the federal procurement data system. We then established a population of undefinitized contract actions at each location and selected a random sample of contract actions to review. Not every location could provide us with a listing of other undefinitized contract actions prior to our site visit, and in some cases there were an insufficient number of such actions to meet our sampling needs. In such cases we reviewed additional letter contracts selected at random to achieve similar sample sizes at each location. A total of 77 undefinitized contract actions were sampled for this review. The six Army, Navy, and Air Force contracting organizations that we selected for our review initiated 70 of the undefinitized contract actions that we reviewed. The National Geospatial-Intelligence Agency initiated 7 of the undefinitized contract actions that we reviewed. Observations made from our review cannot be generalized to the entire population of undefinitized contract actions issued by DOD.

We omitted undefinitized contractual actions for foreign military sales, purchases that did not exceed the simplified acquisition threshold, special access programs, and congressionally mandated long lead procurement contracts since these actions are not subject to compliance with the definitization requirements we were reviewing. We also excluded all undefinitized task orders issued under basic ordering agreements. The majority of pricing and contract terms are established under basic ordering agreements, leaving few terms and conditions to be definitized after award when orders are issued under this type of contract.

At each location, we reviewed contract document files and interviewed officials from the local program office as well as the cognizant contracting officers. In a few cases the contracting officer could not speak to the reasons for definitization delays because that officer was not involved with the award or definitization of the UCA selected for our review. We relied on data provided to us by DOD and the buying commands we visited, which we verified where practical. For example, in determining the length of time to definitize the sampled actions, we verified the data reported in DD350 by tracing the reported award and definitization dates to the contract file documentation. We also verified contract obligation and not-

to-exceed amounts reported in DD350 by reviewing contract file documentation available in hard copy at the sites we visited and electronically from DOD's Electronic Data Access Web-based system.

To obtain insight into the issues surrounding the use of UCAs from a contractor's point of view, we interviewed representatives from four companies who entered into undefinitized contract actions with one or more of the buying organizations that were selected for this review.

We conducted our work from August 2006 through April 2007 in accordance with generally accepted government auditing standards.

Appendix II: Undefinitized Contract Actions Reviewed

	Description of goods or services	Award date	Definitization date	Not-to-exceed amount	Obligation amount at award	Total dollar value at award	Contract/ order pricing type ^a
Air Force							
Aeronautical Systems Center							
1	B-2 aircraft aft deck inner mold kits	2/17/04	8/17/04	\$16,737,000	\$8,368,500	N/A ^b	CPFF
2	Required navigational performance link for C-17 aircraft	9/5/02	12/23/03	5,250,000	2,146,118	N/A ^b	CPAF
3	Common crypto appliqué for F-15 aircraft	2/20/04	7/1/04	1, 366, 402	683,201	N/A ^b	CPFF
4	Enterprise support infrastructure	5/28/04	7/24/04	1,508,938	1,131,704	N/A ^b	FFP
5	Threat Situational Awareness System for B-1 aircraft	12/19/03	6/1/05	23,100,000	10,781,000	N/A ^b	CPFF
6	Aircraft Defense Systems for Army C-37A aircraft	12/8/04	5/2/05	6,038,000	3,019,000	N/A ^b	FFP
7	Receiver/exciter controller upgrade kits	9/30/05	5/18/06	1,287,000	965,250	\$965,250	FFP
8	9 Lynx radar upgrade for Predator unmanned aerial vehicle	7/29/05	9/29/06	13,867,301	10,400,476	10,400,476	FFP
9	Tactical Micro Unmanned Aerial Vehicle improvements	2/8/05	5/18/05	2,202,337	1,101,169	2,202,337	FFP/T&M
10	Receiver/exciter controller upgrade kits for ASARS-2A radar system	5/19/04	2/25/05	5,938,414	4,453,811	8,889,104	FFP
11	Readiness spare package kits for Predator unmanned aerial vehicle	7/1/04	8/24/05	26,427,245	26,427,245	131,028,443	FFP
12	Battlefield Air Targeting Camera Autonomous Micro-Air Vehicles	9/29/05	3/8/06	619,852	309,925	309,925	FFP
Warner Robins Air Logistics Center							
13	Remotely Operated Video Enhanced Receiver upgrade	6/30/04	10/29/04	9,473,313	9,473,313 ^c	9,739,688	CPFF
14	Engineering services for C-130 aircraft	7/22/04	3/20/06	3,240,000	720,000	1,739,934	CPFF
15	Repair of low power color radar	6/2/04	9/28/04	2,900,000	1,450,000	3,648,606	FFP/T&M
16	Upgrade factory test equipment for Joint Helmet Mounted Cueing System	8/2/05	7/27/06	4,102,751	3,077,063	3,077,063	FFP
17	Purchase power supplies for repair	5/3/04	8/11/04	1,500,000	750,000	1,565,250	FFP
18	Multi-functional Information Distribution System initial spares	9/29/05	5/26/06	7,800,000	3,900,000	3,900,000	FFP

**Appendix II: Undefinitized Contract Actions
Reviewed**

	Description of goods or services	Award date	Definitization date	Not-to-exceed amount	Obligation amount at award	Total dollar value at award	Contract/order pricing type^a
19	Replace fire suppression system	3/22/04	6/30/04	2,052,092	1,026,046	1,943,807	FFP
20	Interim support for repair of radar systems for C-130 aircraft	5/5/05	9/28/05	4,372,865	2,186,433	4,372,865	FFP/T&M/CPFF
21	Develop and upgrade transponder software for C-5 aircraft	3/3/04	7/23/04	350,000	175,000	336,814	CPFF
22	Joint Surveillance Target Attack Radar System initial spares	3/25/04	9/30/04	11,840,000	10,763,636	N/A ^b	CPAF
23	Joint Surveillance Target Attack Radar System initial spares for programmed depot maintenance	9/1/05	8/28/06	4,110,537	4,110,537 ^c	N/A ^b	CPAF
24	Replace floor in hangar for C-17 aircraft	1/26/05	2/17/05	1,433,000	716,500	1,425,906	FFP
Army							
Aviation and Missile Command							
25	Periscope head assembly for Bradley fighting vehicle system	2/25/04	6/22/05	2,500,000	1,250,000	1,597,656	CPFF
26	Improved data modems for avionics targeting communication system	8/27/04	6/22/05	3,060,000	1,530,000	2,703,497	FFP
27	Patriot missile rack spares	4/7/05	9/28/05	1,699,323	832,668	1,419,925	FFP
28	Battery assembly	3/3/05	8/05/05	1,227,425	601,438	1,159,705	FFP
29	Integrated sight repair	12/20/04	2/28/06	7,120,000	3,488,800	3,488,800	CPFF
30	Motion picture camera	9/28/05	6/8/06	11,430,000	5,715,000	2,857,500	FFP
31	Auxiliary Power Unit kits and Auxiliary Power Unit spare filter assembly	3/11/05	9/20/05	8,541,860	4,185,511	N/A ^b	FFP
32	Engines for Blackhawk helicopters for State Department	6/2/04	9/28/04	4,118,648	2,018,138	N/A ^b	FFP
33	Auxiliary Power Unit for UH-60 aircraft	7/19/05	9/21/05	2,183,893	2,183,893	N/A ^b	FFP
34	Laser range finders for Avenger vehicles	9/13/04	2/6/06	7,064,844	1,305,691	N/A ^b	FFP
35	Engines for Blackhawk helicopters	1/12/04	9/28/04	46,426,934	22,749,198	N/A ^b	FFP
36	Cargo hooks for CH-47 Chinook helicopters	4/26/05	3/15/06	7,760,000	3,802,400	N/A ^b	FFP
TACOM Life Cycle Management Command							
37	Purchase air conditioning units for trucks located in Southwest Asia	3/5/04	9/24/04	12,321,566	6,160,783	50,222,433	FFP
38	Performance of system technical support services on M707 KNIGHT vehicle program	12/8/04	2/17/05	1,103,200	551,600	14,516,695	CPFF

**Appendix II: Undefinitized Contract Actions
Reviewed**

	Description of goods or services	Award date	Definitization date	Not-to-exceed amount	Obligation amount at award	Total dollar value at award	Contract/ order pricing type^a
39	Conversion of existing contract for remaining system development efforts for Future Combat System	9/30/05	3/28/06	17,350,000,000	219,245,691	254,245,691	CPFF/CPIF
40	Procurement of cargo/troop carrier armor kits and underbody blast protection kits	5/3/04	9/27/04	33,453,860	25,090,387	43,031,578	FFP
41	Rebuild of Medium Tactical Vehicles to repair damage sustained in overseas deployments	2/10/04	8/11/04	20,000,000	10,000,000	31,178,228	CPFF
42	Procurement of the M1117 Armored Security Vehicle	6/30/05	10/31/06	517,660,000	258,830,000	388,245,000	FFP
43	Rebuild of well drilling equipment	3/4/05	7/8/05	200,000	100,000	180,000	FFP
44	Procure ballistic protection armor systems for M-1062 and M-978 fuel tankers	3/31/05	9/22/05	12,840,178	6,420,089	41,030,715	FFP
45	Add-on-armor spare parts for Family of Heavy Tactical Vehicles	2/8/05	12/5/05	1,080,650	540,325	540,325	FFP
46	Procurement of Automatic Fire Suppression System kits for U.S. Marine Corps light armored vehicles	9/29/05	5/26/06	17,827,685	8,913,843	8,913,843	FFP
47	Procurement of armor protection for M-978 fuel tankers	8/2/05	1/26/06	3,559,485	1,779,743	1,779,743	FFP
Navy							
Naval Air Systems Command							
48	Unmanned Aerial Vehicle services for Navy deployments and Gulf oil platform security	4/18/05	9/16/05	14,500,000	7,250,000	28,360,209	FFP
49	Low Rate Initial Production for the 8X10 displays for F/A-18 aircraft	12/12/03	8/9/04	9,075,300	4,537,650	8,157,609	FFP
50	Support of the purchase of Fiber Channel Network Switches for F/A-18 aircraft	3/31/04	10/25/04	3,840,000	1,920,000	12,118,512	FFP
51	Upgrades to the USQ-113 communications receiver/jammer installed on EA-6B aircraft	9/19/05	12/20/06	9,500,000	4,750,000	4,750,000	CPFF
52	Test version of Digital Flight Control System replacement unit for the EA-6B aircraft	6/18/04	2/11/05	1,400,000	700,000	1,855,115	FFP
53	Development and demonstration of upgrades to AN/SPN-46 landing system	2/11/05	6/29/05	4,370,815	2,185,408	4,393,755	CPIF/CPFF

**Appendix II: Undefinitized Contract Actions
Reviewed**

	Description of goods or services	Award date	Definitization date	Not-to-exceed amount	Obligation amount at award	Total dollar value at award	Contract/ order pricing type^a
54	MA-31 aerial targets and related equipment that represent anti-ship cruise missile threats	6/22/04	12/16/04	16,364,000	8,182,000	N/A ^b	FPIF
55	Digital Map Computer and Video Map Computer units for installation on F/A-18 aircraft	3/2/04	9/30/04	9,325,397	6,994,048	N/A ^b	FFP
56	Accelerate the Wing Center Sections improvement for EA-6B aircraft	11/26/03	6/21/04	3,118,057	3,118,057 ^d	N/A ^b	FFP
57	Redesign of specific EA-6B aircraft parts that support upgraded electronic attack capabilities	2/12/04	2/22/05	1,800,000	882,000	N/A ^b	CPFF
58	Implement additional fault isolation for ALQ-218 receiver and wing tip pods on the EA-18G aircraft	9/27/04	9/26/05	7,000,000	3,500,000	N/A ^b	CPAF
Naval Sea Systems Command							
59	Allow contractor to continue detail design and integration efforts on the DD(X) destroyer program	5/25/05	5/28/06	2,951,200,000	123,720,000	136,768,931	CPAF
60	Begin work that supports the start of the DD(X) destroyer detail design activities	9/30/05	12/22/05	53,400,000	26,700,000	26,700,000	CPAF
61	Advanced planning services and long lead items for dry-docking of a Navy aircraft carrier	12/2/03	6/18/04	27,866,659	7,299,338	323,177,007	CPFF/CPIF
62	Design and purchase of Affordable Weapon System guided missile system	3/19/04	8/24/04	22,500,000	11,250,000	51,222,594	CPIF
63	Production and support of Remote Minehunting System to operate from Navy surface ships	9/30/05	10/20/06	30,200,000	14,569,800	14,569,800	FFP/CPFF
64	Support of AEGIS missile guidance system development sites in New Jersey	5/14/04	3/7/05	250,000,000	18,867,529	167,991,564	CPFF/CPIF
65	AN/SPS-48 radar system refurbishment	7/22/05	12/6/05	9,765,598	4,882,799	4,882,812	FFP
66	Design and production of Submarine Rescue System	9/28/05	12/22/06	27,873,202	477,994	477,994	CPFF/FFP
67	AN/SPQ-9B radar systems and related change kit equipment	7/1/04	3/31/05	8,943,742	4,471,871	41,248,398	FFP
68	Migration of Ship Self Defense System software and hardware to Navy compliant open architecture form	5/11/04	8/30/04	38,699,471	10,182,000	26,442,884	CPAF

**Appendix II: Undefinitized Contract Actions
Reviewed**

	Description of goods or services	Award date	Definitization date	Not-to-exceed amount	Obligation amount at award	Total dollar value at award	Contract/order pricing type^a
69	Purchase of AN/BPS-16(V) 4 radar sets	6/22/04	3/25/05	13,266,978	6,633,489	21,040,136	FFP
70	Design and development for Pacific Fleet Tactical Component Network	11/18/04	3/23/06	8,801,797	3,760,400	3,760,400	CPFF
National Geospatial-Intelligence Agency							
71	Commercial data services	9/30/05	7/26/06	9,043,024	4,521,512	4,521,512	CPFF
72	High-bandwidth portable hardware prototype for Secure, Portable, Accessible, Remote, Communications System	8/5/05	9/25/06	5,036,147	2,301,692	N/A ^b	CPFF
73	Low-bandwidth hardware services for Secure, Portable, Accessible, Remote, Communications System	7/26/05	9/25/06	2,934,315	1,467,158	N/A ^b	CPFF
74	Deployable Transit-Case System/Video Processing Capability to support research program	8/23/05	2/16/06	12,000,000	3,414,074	3,414,074	FFP/CPAF/LOE
75	Provide support services at the agency's Virginia facility	12/24/03	8/31/04	24,269,846	3,770,000	54,872,580	CPFF/CPIF
76	Utility assessment and tools development support program	12/1/04	8/19/05	3,300,000	550,000	2,516,000	CPFF
77	Procurement of Mobile Integrated Geospatial Systems vehicles	11/12/03	4/15/04	6,550,000	4,950,000	1,619,973	CPAF

Source: GAO analysis of DOD contract files.

^aCPAF – Cost Plus Award Fee
 CPFF – Cost Plus Fixed Fee
 CPIF – Cost Plus Incentive Fee
 FFP – Firm Fixed Price
 FPIF – Firm Fixed Price Incentive Fee
 LOE – Level of Effort
 T&M – Time-and-materials

^bN/A – Not available from DD350 database

^cThese two UCAs were permitted waivers of 50 percent obligation requirement since they were in support of contingency operations, pursuant to an Air Force memorandum waiving the requirement for actions in support of the Global War on Terror.

^dThis UCA was awarded via a contract modification. The obligations at award for this UCA do not include obligations for the entire contract amount—only for the undefinitized portion.

Appendix III: Comments from the Department of Defense



ACQUISITION,
TECHNOLOGY
AND LOGISTICS

OFFICE OF THE UNDER SECRETARY OF DEFENSE

3000 DEFENSE PENTAGON
WASHINGTON, DC 20301-3000

JUN 13 2007

Ms. Ann Calvaresi-Barr
Director, Acquisition and Sourcing Management
Government Accountability Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Ms. Calvaresi-Barr:

This is the Department of Defense (DoD) response to the GAO report 07-559, "DEFENSE CONTRACTING: Use of Undefined Contract Actions Understated and Definitization Time Frames Often Not Met," dated May 11, 2007, (GAO Code 120637).

The Department has completed its review of the draft report and in general, concurs with GAO's recommendations. We have already taken steps to improve the manner in which we address cost, pricing and financing issues including the manner in which we incentivize the Department's contractors to perform. I have established a Cost, Price and Finance Division within the Defense Procurement and Acquisition Policy organization and as you will see in our attached responses, they are already focusing on current DoD contract financing and funding policies as well as profit/fee policies.

We appreciate the opportunity to review this draft report and provide our comments.

Sincerely,

Shay D. Assad
Director, Defense Procurement
and Acquisition Policy

Enclosure:
As Stated



GAO-07-559 (GAO CODE 120637)

“DEFENSE CONTRACTING: USE OF UNDEFINITIZED
CONTRACT ACTIONS UNDERSTATED AND
DEFINITIZATION TIME FRAMES OFTEN NOT MET”

DEPARTMENT OF DEFENSE COMMENTS
TO THE GAO RECOMMENDATIONS

RECOMMENDATION 1: The GAO recommends that the Secretary of Defense issue guidance to program and contracting officials on how to comply with the FAR requirement to definitize when 40 percent of the work is complete. (p. 16/GAO Draft Report)

DoD RESPONSE: Concur. DoD will issue guidance to clarify the appropriate definitization schedule criteria that apply to contracts for or on behalf of DoD. DoD believes that the GAO’s reference to the FAR requirements for the definitization schedule does not consider the difference in requirements specified for DoD in 10 U.S.C. 2326. While FAR 16.63 requires definitization by the earlier of (1) 180 days after award of the Undefinitized Contract Action (UCA), or (2) before 40% of the work is performed, 10 U.S.C. 2326 provides DoD with different criteria for definitization schedules. The Defense Federal Acquisition Regulation Supplement (DFARS) implements the criteria prescribed in 10 U.S.C. 2326, which requires definitization by the earlier of (1) 180 days after UCA award, or (2) before exceeding 50% of the not-to-exceed price. 10 U.S.C. 2326 permits adjustments to the criteria upon receipt of a qualifying proposal.

The DAR Council has initiated DFARS Case 2007-0011, “Letter Contract Definitization Schedule Criteria” to clarify that DoD contracting officers should use the 10 U.S.C. 2326 definitization schedule criteria located at DFARS 217-7404-3(a).

RECOMMENDATION 2: The GAO recommends that the Secretary of Defense put in place a reporting channel to headquarters that includes information on undefinitized contract actions (UCAs) in place for 180 days or more and that outlines plans and timeframes for definitization. (p. 16/GAO Draft Report)

DoD RESPONSE: Concur. DoD agrees that enhanced oversight is appropriate. We are looking at ways to enhance the efficiency and effectiveness of post-award

contract management, and will consider a policy that requires the Military Departments to enhance oversight of UCAs and to provide periodic reports of over-age UCAs, with remediation plans.

RECOMMENDATION 3: The GAO recommends that the Secretary of Defense supplement acquisition personnel on as as-needed basis to quickly definitize UCAs once they are awarded. (p. 16/GAO Draft Report)

DoD RESPONSE: Concur

RECOMMENDATION 4: The GAO recommends that the Secretary of Defense set forth supplemental guidance to direct contracting officers, where feasible, to obligate less than the maximum allowed at UCA award to incentivize contractors to expedite the definitization process. (p. 16/GAO Draft Report)

DoD RESPONSE: Concur. DoD is currently investigating enhancements to current contract financing and funding policies found in DFARS Part 232. We published a notice in the Federal Register on May 22, 2007 (72 FR 28663) soliciting comments from the public, including any suggestions and recommendations regarding current DoD contract financing and funding policies.

RECOMMENDATION 5: The GAO recommends that the Secretary of Defense set forth supplemental guidance to specify that the effect of contractor's reduced risk during the undefinitized period on profit or fee be documented in the price negotiation memorandum or its equivalent. (p. 16/GAO Draft Report)

DoD RESPONSE: Concur. DoD is currently conducting a study focusing on the area of contract profit/fee policies. On May 22, 2007, DoD published a notice in the Federal Register (72 FR 28663) soliciting input on current DoD contract profit/fee policy. On June 4, 2007, the Director, DPAP, signed a memorandum soliciting similar input from within DoD and OUSD(AT&L) is conducting a study of private sector profit/fee policies and the weighted guidelines guidance. We will incorporate GAO's concerns regarding reduced risk associated with incurred costs vs. higher risk associated with prospective costs in this review.

In addition, we are in the process of reviewing and updating automated tools used to facilitate analysis of profit/fee to ensure that they facilitate appropriate tailoring of risk considerations.

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